IN THE HIGH COURT OF GUJARAT AT AHMEDABAD

SPECIAL CIVIL APPLICATION No 10359 of 2000

For Approval and Signature:

Hon'ble ACTING CHIEF JUSTICE MR.JN BHATT
and
Hon'ble MR.JUSTICE J.M.PANCHAL
and
Hon'ble MR.JUSTICE H.H.MEHTA

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1. Whether Reporters of Local Papers may be allowed to see the judgements? : YES

2. To be referred to the Reporter or not? : YES

3. Whether Their Lordships wish to see the fair copy of the judgement? : NO

4. Whether this case involves a substantial question of law as to the interpretation of the Constitution of India, 1950 of any Order made thereunder? : NO

5. Whether it is to be circulated to the concerned Magistrate/Magistrates,Judge/Judges,Tribunal/Tribunals? : NO

NEW INDIA ASSURANCE CO.LTD.

Versus

HANJER FIBERS LTD.

Appearance:

1. Special Civil Application No. 10359 of 2000

MR PV NANAVATI for Petitioner

MR VIBHUTI NANAVATI for Petitioner

MR TUSHAR MEHTA for Respondent

CORAM : ACTING CHIEF JUSTICE MR.JN BHATT
and
MR.JUSTICE J.M.PANCHAL
and
MR.JUSTICE H.H.MEHTA

Date of decision: 8/04/2003

CAV JUDGEMENT

(Per : ACTING CHIEF JUSTICE MR.JN BHATT)

Whether the dispute about the existence of arbitration clause contained in Insurance Policy would cease to exist on account of passing of receipt of full and final settlement and whether such a dispute is arbitrable or not is the only question, which is in focus for our consideration, determination and adjudication in this reference.

The Larger Bench came to be constituted pursuant to the view taken by the learned single Judge of this Court in Special Civil Application No.10359 of 2000, decided on 6.10.2000, observing that the petition raises important questions which are likely to arise in number of cases and hence, it will be in the fitness of things if the petition is decided by a Larger Bench. Thereafter, learned Chief Justice passed order constituting Larger Bench and that is how this reference came to us.

The petitioner, New India Assurance Company Limited has questioned the legality and validity of the order recorded by the learned Chief Justice under section 11 of the Arbitration and Conciliation Act, 1996 (the Act for short) by invocation of the provisions of Article 226 of the Constitution of India, inter alia, contending that the arbitration clause contained in the insurance policy does not survive and exist as the respondent insured company has passed two receipts of full and final settlement of the claim made by it.

A short resume of facts, giving rise to this petition needs narration for the purpose of examining, appreciating and adjudicating the main controversy between the parties involved in this petition.

The petitioning Insurance Company had issued three insurance policies to the respondent Company,viz :

(i) Fire policy No.11/1003/6050 for a sum of Rs.11,21,10,000 (Rupees Eleven Crores Twenty one lacs and ten thousand only) covering cotton yarn

and the said policy was endorsed in favour of GIIC.

(ii) Policy No.11/220401/00001 for a sum of Rs.6,57,00,000 (Rupees six crores and fifty seven lacs only) covering the stock which was endorsed in favour of SBI and Memon Cooperative Bank.

(iii) Third Policy was issued for a sum of Rs.32,00,000 (Rupees thirtytwo lacs) covering the office/dwelling of the respondent.

The respondent Company lodged claims with the petitioner Insurance Company for the loss sustained by it on account of fire which broke out on 1.4.98 in the premises of the Company, for an amount aggregating to Rs.1.37 crores. Upon the claim being lodged, it was assessed by the Surveyor at Rs.96,45,282/- and the market value was assessed at Rs.95,34,410/-. Obviously the report of the Surveyor was subject to the terms and conditions of the policy.

It is the case of the petitioner Insurance Company that despite breach of the terms of the policy clause 7-B and 7-C, the Company treated the claim of the respondent Company on non-standard basis and offered an amount of Rs.71,50,808/- instead of rejecting the claim of the company on the ground of breach of the terms and conditions of the insurance policies. The aforesaid amount offered by the petitioner Company was accepted by the respondent Company. Therefore, there was a settlement and full satisfaction of the claims. The respondent Company had accepted two cheques aggregating to tune of Rs.71,50,808/- and had passed two vouchers-cum-receipts, which specifically articulated that the amount had been received in full and final settlement of the claim of the respondent Company.

There is no dispute about the fact that arbitration clause has been contained in the insurance policy. The petitioner Insurance Company contended that on account of full and final settlement of the claims, the insurance policy which contained the arbitration clause did not exist and fresh contract of insurance was also made whereas the respondent Company raised dispute by letter dated January 5, 2000, invoking the arbitration clause contained in the insurance policy and claimed the amount as assessed by the Surveyor. The respondent Company, thereafter, by invocation of the provisions of section 11 of the Act, raised dispute by filing objection being

Petition No.16/2000, which came to be fully resisted by the petitioner Insurance Company by filing affidavit in reply raising preliminary objection about the maintainability of such an application, contending that in view of the full and final settlement of the claims made by the respondent Company, no dispute or no cause for claim arose under the arbitration clause and also that as such, arbitration clause ceased to exist. On the other hand, the respondent Company relied on its letter dated 27.9.1999, which is alleged to have been sent with its representative, who was deputed to collect the cheques.

The learned Chief Justice of this Court in exercise of powers under section 11 of the Act passed order on 22.8.2000, on the following grounds :

> "Whether the contents of the two receipts would preclude the petitioner company from raising a further claim and seek arbitration is also a question or issue which the arbitrator is empowered to decide under section 16 of the Arbitration and Conciliation Act, 1996, and therefore considering the fact that there are certain disputed questions of fact arising from the conduct of the parties and correspondence exchanged between the parties by letter dated 27.9.1999 sent by the petitioner company to the respondent (Insurance Company), the forum of arbitration would be better forum for deciding issues of facts and law."

On behalf of the Insurance Company, the main contention raised was to the effect that there was no dispute and therefore, there would not arise any arbitrable issue and the learned Chief Justice has committed serious error in rejecting the preliminary objection. It relied on the decisions which are mentioned in para 4 of the order of the learned single Judge. It was also contended before the learned single Judge that the rejection of preliminary objection would tantamount to taking away the incentive for the Insurance Company to settle the dispute and claims and to offer amounts in full and final settlement. It was, also, contended on behalf of the Insurance Company that though the insurance company could have rejected the claim of the respondent Company on the ground of breach of the terms and conditions of the policy, it took generous and pragmatic view and had agreed to settle the claims and had offered an aggregate amount of Rs.71,50,808/- in full and final settlement of the claims made by the respondent Company under two

policies and the Insurance Company continued the same policy for a further period by charging extra premium instead of cancelling the policy for future period.

However, the learned single Judge found and observed that the petition raised important questions which are likely to arise in number of cases and hence it will be in the fitness of the things if the petition is decided by a Larger Bench. That is how, this Larger Bench came to be constituted by the learned Chief Justice of this Court, as indicated by us hereinbefore.

We have given our anxious thoughts and consideration to the rival submissions and the facts and circumstances and the documents relied on by the parties, as well as, relevant legal profile.

The terms and conditions of the policy contain arbitration clause No.13 providing for appointment of agreed common arbitrator or in the alternative two arbitrators to be nominated by each of the parties. The learned Chief Justice of this Court has observed in his order dated 22nd August, 2000, after considering the preliminary objections raised by the Insurance Company that under section 16 of the Act, the Arbitrator is, also, empowered to decide the preliminary point and issue raised by the Insurance Company and, therefore, abstaining from expressing any final opinion on the said question, leaving it open to the parties to raise that question before the Arbitrator or Arbitrators, called upon the parties to propose the name of one common Arbitrator or two Arbitrators to be nominated by each one of them. It appears that in view of the writ petition filed by the Insurance Company, further proceedings could not be taken.

It is a settled proposition of law, by now, at this stage, that the order of the learned Chief Justice or his nominee passed under section 11 of the Act is amenable to the writ jurisdiction under Article 226 of the Constitution of India. Therefore, this petition under Article 226 of the Constitution of India, at the instance of the Insurance Company, challenging the order dated 22.8.2000 of the learned Chief Justice passed under section 11 of the Act making reference to arbitration is competent and the preliminary objection raised by the petitioning Insurance Company, as such, is not overruled but is referred to Arbitrator or Arbitrators. In this connection, it would be pertinent to mention the following paragraph from the order of the learned Chief Justice :

"Whether the contents of the two receipts would preclude the petitioner company from raising a further claim and seek arbitration is also a question or issue which the arbitrator is empowered to decide under section 16 of the Arbitration and Conciliation Act, 1996. I, therefore, abstain from expressing any final opinion on the said question leaving it open to the parties to raise that question before the arbitrator or arbitrators."

It is true that section 16 does not take away the powers of the learned Chief Justice under section 11 of the Act to decide whether a dispute is arbitrable or not. It was, therefore, open for the learned Chief Justice to decide the preliminary issue or leave it open to the parties to raise before the Arbitrator or Arbitrators. The learned Chief Justice opted the latter option out of two for the reason that there are certain disputed questions of fact arising from the conduct of the parties and correspondence exchanged between them and, therefore, it was thought expedient by the learned Chief Justice that the forum of arbitration would be better for deciding such issues of facts and, also, of law.

In Chapter IV of the Arbitration and Conciliation Act, 1996, provisions are made with regard to jurisdiction of arbitral tribunals. Section 16 empowers the arbitral Tribunal to rule on its jurisdiction. It is very relevant and material and is a direct answer to the question posed by the learned single Judge in para 5 in the reference order. Section 16 reads as under:

"16. Competence of arbitral tribunal to rule on its jurisdiction.

(1) The arbitral tribunal may rule on its own jurisdiction, including ruling or any objections with respect to the existence or validity of the arbitration agreement, and for that purpose -

(a) an arbitration clause which forms part of a contract shall be treated as an agreement independent of the other terms of the contract, and

(b) a decision by the arbitral tribunal that the contract is null and valid shall not entail ipso jure the invalidity of the arbitration clause.

(2) A pleas that the arbitral tribunal does not have jurisdiction shall be raised not later than the submission of the statement of defence; however, a party shall not be precluded from raising such a plea merely because that he has appointed, or participated in the appointment of, an arbitrator.

(3) A plea that the arbitral tribunal is exceeding the scope of its authority shall be raised as soon as the matter alleged to be beyond the scope of its authority is raised during the arbitral proceedings.

(4) The arbitral tribunal may, in either of the cases referred to in sub-section (2) or sub-section (3), admit a later plea if it considers the delay justified.

(5) The arbitral tribunal shall decide on a plea referred to in sub-section (2) or sub-section (3) and, where the arbitral tribunal takes a decision rejecting the plea, continue with arbitral proceedings and make an arbitral award.

(6) A party aggrieved by such an arbitral award may make an application for setting aside such an arbitral award in accordance with section 34."

It is evident and explicit that sub-section (1) of section 16 prescribes competence of arbitral tribunal to rule on its jurisdiction. Chapter IV has only two sections, like that section 16 and 17. Section 16 deals with matters of jurisdiction, nature and validity of the arbitration clause. In fact, this is a new and very important section which corresponds to Article 16 of the UNCITRAL Model Law. It can, also, be very well visualised that section 16(1) to (5) materially and substantially correspond to sections 30(1) (a), 30(1)(c), 31(1), 31(2), 31(3) and 67(2) of the English Arbitration Act, 1996.

Sub-section (1) of section 16, evidently, empowers arbitral tribunals to rule on its own jurisdiction including any objections with respect to the existence or validity of the arbitration agreement. Obviously, that decision would be subject to the ultimate determination of the court on judicial review as provided under section 34 of the Act. It is true that, ordinarily, as a rule,

an arbitrator cannot clothe himself with power to decide the issue pertaining to his own jurisdiction. Nevertheless, arbitrator could be empowered or invested with powers by the parties to decide those questions, as for instance, by a collateral or separate agreement which will be effective and operative.

A student of Indian or English Law would, always be surprised with such empowerment about jurisdiction to the arbitral tribunal because until 1996, the English as also Indian Law, has taken a view that arbitral tribunal cannot be invested with competence to decide its jurisdiction or to decide the objection about the existence or validity of an arbitration agreement. In other words, hitherto, the English Law has been that arbitral tribunal cannot be the adjudicator on its own jurisdiction. For the first time, clear provision came to be incorporated in Indian Law in section 16 of the Act 1996. It may be mentioned that the final decision as to the substantive jurisdiction of the Tribunal would rest with the Court. Section 34 of the Act provides recourse against arbitral award.

Since the arbitral tribunal is competent to rule on its own jurisdiction including ruling of any objection with regard to existence or validity of the arbitration agrement, the order of the learned Chief Justice with regard to preliminary objection and direction that the preliminary objection to be decided by the arbitral Tribunal under section 16 of the Act of 1996 without expressing any final opinion on the said question and leaving it open to the parties to raise that question before the arbitrator or arbitrators could not be said to be vulnerable or in any way unjust, unreasonable, arbitrary or invalid requiring interference in exercise of constitutional writ jurisdiction. The parties aggrieved by an arbitral award, after rejection of such plea of jurisdiction or validity or existence of the arbitration agrement can challenge the same by invocation of the provisions of section 34 of the Act. Section 34 reads as under:

"34. Application for setting aside arbitral award.

(1) Recourse to a court against an arbitral award may be made only by an application for setting aside such award in accordance with sub-section (2) and sub-section (3).

(2) An arbitral award may be set aside by the

court only if -

(a) the party making the application furnishes proof that -

(i) a party was under some incapacity, or

(ii) the arbitration agreement is not valid under the law to which the parties have subjected it or, failing any indication thereon, under the law for the time being in force; or

(iii) the party making the application was not given proper notice of the appointment of an arbitrator or of the arbitral proceedings or was otherwise unable to present his case; or

(iv) the arbitral award deals with a dispute not contemplated by or not falling within the terms of the submission to arbitration, or it contains decisions on matters beyond the scope of the submission to the arbitration:

Provided that, if the decisions on matters submitted to arbitration can be separated from those not so submitted, only that part of the arbitral award which contains decisions on matters not submitted to arbitration may be set aside; or

(v) The composition of the arbitral tribunal or the arbitral procedure was not in accordance with the agreement of the parties, unless such agreement was in conflict with a provision of this Part from which the parties cannot derogate, or, failing such agreement, was not in accordance with this Part; or

(b) the court finds that -

(i) the subject - matter of the dispute is not capable of settlement by arbitration under the law for the time being in force, or

(ii) the arbitral award is in conflict with the public policy of India.

Explanation : without prejudice to the generality of sub-clause (ii) of clause (b), it is hereby declared, for the avoidance of any doubt, that an award is in conflict with the public policy of India if the making of the award was induced or affected by fraud or corruption or was in violation of section 75 or section 81.

(iii) an application for setting aside may not be made after three months have elapsed from the date on which the party making that application had received the arbitral award or, if request had been made under section 33, from the date on which that request had been disposed of by the arbitral tribunal:

Provided that if the Court is satisfied that the applicant was prevented by sufficient cause from making the application within the said period of three months, it may entertain the application within a further period of thirty days, but not thereafter.

(iv) On receipt of an application under sub-section (1), the court may, where it is appropriate and it is so requested by a party, adjourn the proceedings for a period of time determined by it in order to give the arbitral tribunal an opportunity to resume the arbitral proceedings or to take such other action as in the opinion of arbitral tribunal will eliminate the grounds for setting aside the arbitral award."

It is very clear from the aforesaid provisions that an aggrieved party is entitled to recourse to a court against an arbitral award, by making an application for setting aside such an award in accordance with sub-section (2) and sub-section (3) of section 34. The order for setting aside or refusing to set aside an arbitral award under section 34 is again appealable by reason of section 37 of the Act. Therefore, the discretionary exercise of power in referring the matter to arbitral tribunal cannot be said to be unjustified. The view which we are inclined to take is, also, very much reinforced by a Constitution Bench decision of the Hon'ble Supreme Court in the case of Konkan Railway Corporation Ltd. v. Rani Construction Pvt. Ltd., (2002) 2 Supreme Court Cases 388.

The mechanism provided in 1996 Act aims to limit the judicial intervention in arbitral proceedings. There is substantial departure from the Act of 1940. 1940 Act provided for three recourses against an award, (a) rectification, (b) remission and (c) setting aside. Those recourses are now grouped into two. Arbitral tribunal and so also the parties can tackle the subject of rectification without intervention of the court. In the working of arbitral proceedings during operation of

1940 Act, there has been great dissatisfaction about the arbitral process under the said Act. It has, also, been successfully, noticed that there were widespread abuses and misuse of arbitral process. In the case of M/s.Guru Nanak Foundation v. M/s.Rattan Singh & sons, AIR 1981 SC 2075, the following observations made by the Hon'ble Supreme Court are pertinent.

> "Interminable, time consuming, complex and expensive court procedures impelled jurists to search for an alternative forum, less formal, more effective and speedy for resolution of disputes avoiding procedural claptrap and this led them to Arbitration Act, 1940 (Act for short). However, the way in which the proceedings under the Act are conducted and without an exception challenged in Courts, has made lawyers laugh and legal philosophers weep. Experience shows that law reports bear ample testimony that the proceedings under the Act have become highly technical accompanied by unending prolixity, at every stage providing a legal trap to the unwary. Informal forum chosen by the parties for expeditious disposal of their disputes has by the decisions of the courts been clothed with "legalese" of unforeseeable complexity."

It was also observed by the Apex Court in one of the Special Leave Petitions that arbitration is dreaded more than a suit by honest man. The Apex Court was constrained to make caustic remarks on the working of 1940 Act in Food Corporation of India v. Joginderpal Mohinderpal, AIR 1989 SC 1263. It was noticed and observed by the Apex Court in the said case that the law of arbitration should be simple, less technical and more responsible to the actual realities of the situations. It was also noticed in the said case that the working of the arbitral Tribunal should be responsive to the canons of justice and fair play and make the arbitrator adhere to such process and norms to create confidence. The purpose of arbitration proceedings was to cut-short delay and to provide speedy and less expensive justice. But it was not accomplished. It is in this context, adverse remarks and comments against the working of 1940 Act came to be made in the 210th Report of the Public Accounts Committee of the Fifth Lok Sabha and the 9th Report of the Public Accounts Committee of the Sixth Lok Sabha. The Government of India, therefore, referred the matter to the Law Commission of India for its examination and report in 1977. The 76th Report of the Law Commission

under the Chairmanship of Hon'ble Mr.Justice H.R.Khanna submitted to the Government on 9th November 1978, recommended the necessity to amend 1940 Act to suit the felt necessities of the time including developing economy of the country. Of course, then the wind and wave of philosophy of globalisation was even far from being sighted and UNCITRAL wonderful farsightedness !

It will be interesting to mention here that many public service oriented institutions of trade, industry, commerce and eminent jurists and lawyers and scholars also felt for drastic changes. Again 13th Law Commission undertook further examination of its recommendations. The Malimath Committee constituted by the Government of India on the recommendations of the Chief Justice Conference recommended number of alternative modes and reforms in the 1940 Act. Even the United Nations Commission on International Trade Law (UNCITRAL) came to be established by the General Assembly resolution for the purpose of the promotion of the progressive harmonisation and unification of the law of international trade as its objectives.

Several countries enacted law to give legal force to the Model Law within their jurisdiction. It is in this context, the 1996 Act came into existence which is indubitably much more progressive than the repealed 1940 Act. It has provided unified formula for both international commercial arbitration and domestic arbitration and consolidated the entire law on arbitration. Thus, the new Act recognizes maximum possible party autonomy in matters relating to arbitration. It is also designed to cut-short delay and provide speedy justice.

The learned single Judge instead of making a reference to a Larger Bench by formulating a question or questions has referred the entire petition to be decided by a Larger Bench. In view of the aforesaid discussions, factual profile emerging from the record and keeping an eye on the provisions of 1996 Act, and particularly the provisions of section 16 read with section 34, we are of the opinion that the view taken by the learned Chief Justice while exercising his powers under section 11 of the 1996 Act and referring the matter to the arbitral tribunal keeping the preliminary issue open and permitting the parties to raise such a question before the arbitral tribunal, is quite legal, valid and acceptable. Therefore, the order of the learned Chief Justice in an application under section 11 being Petition under Arbitration Act No.16 of 2000, requires no

interference in this petition under Article 226 of the Constitution of India.

Consequently, the petition shall stand dismissed. The Registry is directed to place the matter before the learned Chief Justice or his nominee for further proceedings, without any avoidable delay. Rule discharged.

(J.N.Bhatt, Acting CJ)

(J.M.Panchal, J.)

(H.H.Mehta, J.)

(vjn)